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UNCLAS SECTION 01 OF 03 SANTO DOMINGO 005740

SIPDIS

SENSITIVE

DEPT FOR WHA, WHA/CAR, WHA/EPSC, EB/ESC; DEPT PASS
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FOR ILAB;SOUTHCOM ALSO FOR POLAD;TREASURY FOR OASIA-LCARTER

E.O. 12958: N/A
TAGS: DR ECON ENRG PGOV EINV
SUBJECT: DOMINICAN ELECTRICITY: THE LAZARUS EFFECT

REF: SANTO DOMINGO 01606

¶1. Summary (SBU) The Dominican electrical sector is still in great difficulty. Generation is running consistently below peak demand. Blackouts occur regularly, although they are less prolonged than in the last days of the Mejia administration. The government is keeping the lights through the end of the year on with money borrowed from Dominican commercial banks. The strapped Dominican government is rationing payments to electricity producers, providing just enough for purchases of increasingly expensive fuel. USAID and the World Bank are supporting a government effort to define a stabilization plan. With no sign of any profit until at least the end of 2005, U.S. firm AES is close to selling off its generating and distributing operations.

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Chunky payments
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¶2. (U) When Leonel Fernandez took office on August 16, power output had been running as low as 700 megawatts (MW), less than half of the daily peak demand of around 1600 MW. This meant 12-20 hour blackouts across the country. The new administration obtained a USD 65 million loan to purchase fuel for the sector, coordinated by Santo-Domingo-based Banco Popular. Most was to purchase fuel (USD 50 million) and the rest was for bottled cooking gas (USD15 million). The plan is to spend roughly USD 10 million a month on fuel for power plants. One unforeseen issue with the program is that the generators need to purchase fuel in bulk and these limited payments are not enough to buy a full shipment. The consequence has been that generators have to hold the cash until they have enough for a full shipload -- purchased on the spot market at a premium. The first disbursements from the loan were made in September.

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Current generation
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¶3. (U) The most recent statistics show that the system is typically producing between 1100 and 1200 megawatts in the early morning hours. This is similar to or better than what we've seen for much of the past year, and it means that much of the country suffers sporadic blackouts. The system is decapitalized, burdened with debts of between USD 400m and 450m. Distributors fail to collect sufficient funds with which to pay generators, due to the continued high rate of theft and the simple refusals to pay by many users. The government consistently fails to cover promised subsidies. Without payments the generators cannot rapidly replenish the imported fuel needed for generating the electricity.

¶4. (U) Currently, distribution companies, Edeste (run by AES) and government-owned Edenorte and Edesur (formerly run by Union Fenosa of Spain), lose about 40 percent of the electricity that they distribute, a quarter of that from technical losses and the rest coming from theft. Collections for power delivered and billed range from 66-77 percent for the distribution companies. Users have few incentives to pay and continue to tap into lines illegally or ignore bills. Encouraging the theft and hindering collections are rules that prohibit distributors from cutting off power for non-payment; companies have to pass through an arduous legal process involving the courts.

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Trying to renegotiate, again
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¶5. (U) Rhadames Segura, Director of Dominican electricity agency CDEEE has said publicly that the government intends to re-negotiate the contracts with the generating companies. Still starved of cash, it has nothing to offer the companies in those talks in exchange for a permanent lowering of contract rates. The figure previously negotiated with most generators in the Madrid Accords, now essentially defunct, was about USD 200, to be financed by the World Bank -- but the government's failure to stay on track with the IMF blocked that lending program. A USAID-supported study on the

prospects for the sector is almost ready for discussion with sector participants. It will offer all of them, including U.S. companies such as AES, Cogentrix, El Paso and Seaboard, a better basis for determining whether they will want to renegotiate.

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AES - Getting Out of Dodge
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¶6. (SBU) Julian Nebreda of AES-Dominican Republic and Blair Thomas, Managing Director of the Trust Company of the West (TCW), a California based private financial services firm, told the Ambassador on July 28 that AES would sell its 50 percent holding of electrical distribution company Edeste for an undisclosed amount. AES will continue to manage Edeste for TCW. On October 8, George Dewey, Chief Commercial Officer of Coffeyville Resources of Kansas City, told the Ambassador of interest in purchasing other AES assets - - the 500 MW complex named AES Andres and Los Mina and its Itabo partnership with El Paso and Globaleq with up to 650 MW of generation capacity.

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Energy Shortage Leads to Expensive Schemes
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¶7. (SBU) Press accounts have the GODR inquiring about the purchase of two 500 MW coal burning power plants that were originally intended for India but are waiting in Houston for a buyer. Each power plant costs USD 750 million and would notionally be located on the north side of the country near Monti Cristi. Smith Enron (future name: Prisma) currently has the only major power plant in the north, with 185MW of capacity in Puerto Plata. The proposal to import more generating capacity is a non-solution. At the moment the Dominican Republic has plenty of capacity - - the compound problem is debt, non-collection, a lack of direction and uncertainty about the government's intentions.

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Stabilizing Dominican Electricity until December 2005
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¶8. (U) USAID in collaboration with the World Bank is financing work on a plan to stabilize the Dominican electrical sector over the period running to December 2005. The study is under discussion with sector participants and will probably be submitted to President Fernandez later this week (October 20-22). The plan is a minimal proposal, intended to keep the lights on over the next 18 months: it does not address the issue of debt repayment to the generating or distribution companies. It is focused initially on the need to stop the continued accumulation of losses. It includes the rationale and recommendations for raising rates, reducing technical losses and piracy, increasinge collections and reducing subsidies. If consensus is possible, this aproach would be the basis for seeking multilateral bank financing to cover a financing gap estimated at 200-300 million dollars. The draft plan does not pretend to be a cure-all; it would require a technical and financing miracle to get this Lazarus to rise and walk. Instead, the plan aims at providing electricity to meet 75 percent of demand expected over a 24-hour period. To help encourage payment, the proposal recommends rationing power and allocating it to areas of the country according to their records of payment.

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Intrasector Debt Drags On
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¶9. (U) There is currently an accumulated intrasector debt of USD 400m to 450m for the Dominican electricity grid. In 2002 the distribution companies were able to collect about 12 cents of the 14 cents it cost to generate electricity. By 2003 the three distributors were able to collect only 7 to 8 cents while the cost of generation rose to between 16 to 18 cents a KWH. This huge discrepancy resulted from several factors: tariffs paid to generators are fixed in dollars, as are fuel prices; the peso rapidly devalued from 18 pesos to 55 pesos to the dollar over the last two years without no corresponding adjustment of peso tariffs; the government made a political decision in April 2003 to subsidize electricity, despite its lack of resources to cover these payments; the government's response to massive bank frauds in 2003 led to a multiplication of public sector debt and further hampered its ability to pay; and the fact that more than 50 percent of users do not pay their electric bills. Private and public sector collections by distribution

companies are equivalent to only about 48 percent of potential.

¶10. (U) There is general agreement on the level of debts except for a dispute between AES-managed Edeste and the government corporation CDEEE. A 50 million dollar difference in calculations is due to two factors: a dispute on whether Edeste should pay for government-installed substations, and the cost of the government-imposed lag of two months between billings and receipt of payment. Edeste maintains that standard business practice allows for no more than a 30-day payment delay and that the CDE should pay for the financing cost of the extra month. The lag is especially costly because of the sharp increase in peso interest rates after mid-2003 and the uncertainties of the exchange rate.

¶11. (U) Drafted by Mark Kendrick

¶12. (U) This report and others can be read on the SIPRNET at http://www.state.sgov.gov/p/wha/santodomingo/ index.cfm along with extensive other current material.
HERTELL